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SWEDWATCH

POLICY PAPER
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Time for climate leadership in carbon-free export finance

– An opportunity for Sweden

Summary

In Sweden and elsewhere, export credit policies have not fully aligned with the climate goals of the Paris Agreement or with scenarios on net zero emissions pathways. Despite recent policy changes to limit support for coal, oil and gas extraction and exploration, current Swedish export credit policies allow actors in the export credit system to promote and underwrite projects in the oil and gas value chain, including power plants, refineries, pipelines, and the transport and storage of fossil fuels. Yet support for fossil fuel energy projects is at odds with Sweden's climate policies in other areas, and with Sweden's ambition to be one of the world's first fossil-free welfare nations. This brief argues that Sweden's export credit policies should align with its climate policies – including the goal of a fossil-free Sweden and the temperature goals of the Paris Agreement – while recognising the need for (and ensuring) a just transition. Sweden should also promote stricter policies on export support to the oil and gas industries in international fora, such as the Organisation for Economic Co-operation and Development (OECD) and the United Nations (UN) Climate Change Conference.

RECOMMENDATIONS TO THE GOVERNMENT OF SWEDEN

- **Domestically, ensure coherence in all aspects of climate policy and adopt a whole-of-government approach to climate change. This includes ending export finance support to overseas fossil fuel energy projects and recognising the need for a just transition;**
- **Internationally, help establish a coalition of countries committing to stop export financing of fossil fuel energy projects ahead of the November 2021 UN Climate Change Conference (COP26) in Glasgow;**
- **Within the OECD, advocate for the introduction of a new Sector Understanding on restrictions to oil and gas export finance, as well as for strong climate provisions throughout the OECD Arrangement.**

Background: climate change and the role of financial actors

Scientists agree that to mitigate the worst effects of global warming, greenhouse gas emissions should quickly decline to net zero by 2050. To achieve this, signatories of the 2015 Paris Agreement have committed to making "financial flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development"[1] and solicited the help of non-state stakeholders, including financial institutions, to "address and respond to climate change."[2] Business and financial actors thus have a clear role to play in addressing the risks arising from climate change.

According to the August 2021 Sixth Assessment Report (AR6) of the UN's Intergovernmental Panel on Climate Change (IPCC), global warming could exceed 2 °C as soon as 2040–2050 unless strong climate mitigation measures are quickly implemented.[3] According to the AR6, only scenarios with very low or low greenhouse gas emissions declining to net zero around or after 2050 are likely to avoid global warming of more than 1.5 °C and 2 °C, respectively. The findings of the AR6 confirm, once again, the urgency of strong policy action to limit greenhouse gas emissions.

In its report *Net Zero by 2050: A roadmap for the global energy system*, the International Energy Agency (IEA) concludes that the global pathway to net zero emissions by 2050 requires "all governments to significantly strengthen and then successfully implement their energy and climate policies."[4] According to the agency's analysis, the pathway that is "the most technically feasible, cost-effective and socially acceptable" leaves no room for the development of new oil or natural gas fields, and unabated[I] coal and oil power plants (i.e., those that do not capture and store carbon) need to be phased out as soon as possible. Electricity generation by unabated natural gas should decrease beginning in the mid-2020s;[5] by 2050, global natural gas use should be reduced by 55 percent compared to 2020.[6] The IEA scenario depicts a narrow path to net zero emissions and a series of milestones including the phaseout of fossil fuels and the large-scale implementation of renewable energy and energy efficiency technologies. These milestones require significant readjustments in all sectors of society, including export finance and export credit agencies.

Nonetheless, the current global climate policy landscape differs starkly from net zero scenarios: despite a temporary decline due to the Covid-19 pandemic, greenhouse gas emissions remain unsustainably high, and investments in the current and planned production of fossil fuels are not aligned with the 1.5 °C (or well below 2 °C) temperature goal of the Paris Agreement.[7]

Export finance and climate change

Export credit actors provide credits, guarantees, or loans to exporting companies, and thus enable export deals that would have otherwise been more difficult, costly, or impossible to execute. Export credit agencies thus play a crucial role in financing and determining the development of energy technologies in the Global South. Since national governments typically regulate these agencies, policy coherence would require aligning policies governing trade promotion, export finance, overseas development aid and direct foreign investments with exporting countries' climate goals and international commitments, such as those of the Paris Agreement. However, while export credit agencies in some countries have begun to align their activities with climate goals, data from the non-governmental organisation (NGO) Oil Change International show that such agencies remain some of the largest international public financiers of fossil fuel energy projects.[8] This is troubling, given the tight timeframe to reduce emissions outlined in the IPCC's AR6: continued support for investments in fossil fuel energy projects can lead to global warming of

I The term "unabated" refers to the combustion of fossil fuels without carbon capture and storage which can ensure the long-term sequestration of carbon dioxide from the atmosphere.

more than 2 °C and to "carbon lock-in"[II] in low-income countries for many years to come, and makes their energy mix overly reliant on fossil fuels and incompatible with the 1.5 °C temperature goal. Furthermore, fossil fuel energy projects frequently lead to adverse impacts on the environment and public health.[9]

Policies governing export finance and the climate transition in Sweden

Poor policy coherence between export finance policies and national and international climate commitments has only recently received attention. Much remains to be done to align the activities of export credit agencies with climate goals. In 2015 Sweden announced its intention to become "one of the world's first fossil-free welfare nations"[10], and in 2017 it adopted a net zero climate policy framework.[11] However, the Swedish government has not yet fully aligned its policies governing the export credit agency Exportkreditnämnden (EKN) and the state-owned export finance bank AB Svensk Exportkredit (SEK) with climate goals. Both have been criticised for guaranteeing and financing export projects that contribute to adverse impacts on health and the climate.[12] [13] In 2019 and 2020, EKN issued guarantees associated with oil and gas worth 965 million Swedish krona (kr)[14] – and for 120 million kr in the first four months of 2021.[III]

As part of a new export strategy focusing on clean-tech exports and their potential contribution to climate change mitigation in export markets, in 2019 the Swedish government adopted new policies to begin aligning the country's export credit system with its climate goals.[15]

The new export strategy commits to phasing out export finance for the extraction and prospecting of fossil fuels by 2022. It further mandates actors in the Swedish export credit system to evaluate how export credits can help transition to climate-resilient development and avoid carbon lock-in effects in other countries. In September 2020, EKN issued a report[16] recommending that the Swedish export credit system enhance support for business deals that contribute to the climate transition and increase transparency on sustainability and climate areas. The December 2020 appropriation letter (*regleringsbrev*) from the government to EKN reflected these recommendations.[17]

Consistent with the report's recommendations and the appropriation letter, in 2020 EKN and SEK adopted criteria to evaluate support for projects that have the potential to increase greenhouse gas emissions, including by assessing whether such projects have the potential for a low-carbon transition by 2030, and whether they are compatible with global net zero emissions by 2050. In 2020, ahead of the deadline set out by the export strategy, EKN updated its sustainability policy[18] to exclude business activities related to coal, unconventional oil and gas, or new developments of oil and gas fields from export finance support.[19] In August 2021 EKN and SEK announced that a scientific climate council had been established to provide advisory support to EKN and SEK to align the Swedish export finance system with the Paris Agreement's 1.5 °C goal.[20]

However, despite these positive policy developments and the strategy to provide more support for renewable energy projects, the government does not require Swedish export credit actors to phase out export finance for projects throughout the fossil fuel value chain. Consequently, EKN's and SEK's policies still allow them to finance projects such as refineries, pipelines, and oil and gas power plants.

International context

While each state regulates the activities of its own national export credit agencies, international frameworks govern various aspects of export credits, including climate change and fossil fuels. However, these frameworks fail to ensure that

II The Stockholm Environmental Institute defines carbon lock-in as a situation in which "once certain carbon-intensive investments are made, and development pathways are chosen, fossil fuel dependence and associated carbon emissions will be 'locked in', making it more difficult to move to lower-carbon pathways."

III See the Appendix. EKN's exposure to fossil fuel energy projects between January 2019 and April 2021 amounted to 1% of EKN's total transactions.

export credit agencies are fully aligned with international climate goals; they instead set minimum terms to avoid supporting projects with the highest climate impacts.

For instance, the Organisation for Economic Co-operation and Development (OECD) adopted already in 1978 an "Arrangement"[21] to create a level playing field for government-supported export credits, which includes "Sector Understandings" on different topics, including coal-fired electricity generation (known as the Coal-Fired Sector Understanding, CFSU[22]) in which member countries commit to refrain from providing export support to coal power plants over a certain capacity. However, the CFSU contemplates only limited exemptions on what types of fossil fuel energy projects are to be excluded from export finance support; essentially it merely encourages exporters and buyers of coal-fired power plants to move from "low-efficiency" towards "high-efficiency" coal burning technologies.

Within the European Union (EU), the Foreign Affairs Council has agreed to discourage further investments in fossil fuel-based energy infrastructure projects in third countries and called for an end to financing of new coal infrastructure, and to promote a global phaseout of harmful fossil fuel subsidies.[23] European regulation 1233/2011[24] effectively makes the OECD arrangement legally binding for EU member states' export credit agencies, and sets out reporting measures – including how agencies should assess environmental risks.

In April 2021, Sweden, Denmark, the Netherlands, France, Spain, Germany, and the United Kingdom (UK) created the Export Finance for Future (E3F) initiative[25] that commits them to align export finance to climate targets. Yet the initiative's commitments fall short of a comprehensive exclusion of export finance to all fossil fuel energy projects. While the signatories agreed to stop export finance directed to coal and coal power, they adopted weaker commitments in relation to oil and gas, such as initiating a review of how best to phase out export finance to fossil fuel energy projects. Above all, the E3F initiative lacks clear timelines and targets.

Similarly, in May 2021, the G7 countries adopted ambitious but vaguely defined commitments "to ensure that financial flows from [public financial institutions] are aligned with the goals of the Paris Agreement". G7 countries also agreed to "take concrete steps" to end financing of coal power projects by the end of 2021, and to begin phasing out support for "carbon intensive inter-

An obligation to reduce emissions

It is increasingly recognised that governments and other state actors have a legal obligation to take adequate action to mitigate climate change. A legal opinion[28] focussing on the roles and responsibilities of export credit agencies in mitigating climate change was released in May 2021 at the behest of the international NGO Oil Change International.

The opinion states that export credit agencies' continued support for fossil fuel energy projects in the form of export credits is in principle not compatible with international law obligations, and that such agencies should adopt timelines to decrease and phase out support for fossil fuel energy projects. This legal opinion maintains that states have a due diligence obligation under international law to avoid causing significant environmental harm and to protect human rights, which in turn implies efforts to reduce emissions.

The Dutch Supreme Court espoused a similar argument in December 2019 when it upheld a claim brought by Dutch NGO Urgenda requesting that the Dutch government review its greenhouse gas emissions reduction targets.[29] While the Court recognised the uncertainties and complexities of climate change mitigation, and acknowledged that a single state cannot solve climate change on its own, it maintained that the Dutch state has an individual responsibility to mitigate climate change, regardless of measures adopted by other states.

Climate change litigation has increased in recent years: claims against state and business actors are constantly breaking new legal ground, and governments and export credit agencies may soon face litigation for providing export finance support to fossil fuel energy projects overseas during a climate crisis.

national fossil fuel energy, except in limited circumstances."[26]

At the time of writing, the UK's March 2021 policy on export credits and climate is the only one contemplating a blanket exclusion of the fossil fuel energy sector overseas from export finance. [27] The UK policy states that UK will no longer engage in trade promotion activities and provide export finance support related to fossil fuels, but includes exemptions for gas-powered generation under the fulfilment of certain conditions as well as a one-year transition period for small and medium-sized exporters.

A just transition in export finance

The transition to a low-carbon and climate-resilient economy is generally thought to have the potential to stimulate economic growth and create employment opportunities.[30] However, climate transition policies, including efforts to align export finance with climate goals, can also adversely impact industry sectors, companies, communities and jobs.[31] It is hence important to manage the impacts of policy change using a just transition perspective to ensure that equity issues are addressed. Transitions that adopt a rights-based approach – and take into account the impacts on vulnerable workers, families and communities affected by policy changes – are arguably more likely to succeed.[32] In other words, successful climate policies can effectively manage the risks of transition while ensuring that equity issues are addressed.

Export credits can generate negative impacts and equity issues both domestically and abroad. Domestically, new business and employment opportunities created by the climate transition will likely be created in sectors and regions other than those most impacted by the low-carbon transition.[33] At the same time, a study evaluating export finance support for domestic energy jobs in the UK, which has a sizeable oil and gas industry, found that support for renewable technologies is more effective at creating jobs than support for the oil and gas sectors, mainly because renewables are more labour intensive than fossil fuels.[34] In addition, the study found that phasing out export finance to fossil fuel energy projects would not overly affect UK domestic jobs.

Fossil fuel energy infrastructure is sometimes considered necessary for development in countries and regions with poor energy infrastructure, or where access to energy is lacking.[35] However, the downward cost trends of renewable energy, the adverse impacts of fossil fuels on health, and considerations about communities' energy independence demonstrate that fossil fuels are far from the best solution to guarantee development and access to energy in least developed countries. On the contrary, continued investment in fossil fuel infrastructure has the potential to lock low- and middle-income countries into carbon-dependent pathways, exposing them to transition risks[IV] and the risk of creating stranded assets and stranded communities. Multilateral and development finance institutions focused on reducing poverty and promoting sustainable development have enacted policies that cap financing of fossil fuel energy projects. Such policies are motivated by a recognition that the failure to mitigate climate change will disproportionally affect marginalised groups in least developed countries[V].

From a just transition perspective, new trade promotion and export credit policies should include provisions to support affected workers, families, regions and communities, including through re-skilling, education and research, and support to impacted industry sectors.[36] For example, the recent UK policy change, which prohibits the provision of new direct financial or promotional support for overseas fossil fuel sectors, other than in exceptional circumstances, was accompanied by measures to support industry in this transition, including a grace period for small and medium-sized enterprises, as well as a renewed focus on the trade opportunities arising from new energy markets. From the perspec-

IV Transition risks can be defined as the risks arising from changes in policies, practices, and technologies, as government and societal actors take regional or global action to constrain carbon-intensive activities.

V For example, Swedish development finance institution Swedfund, which has a mandate to invest to reduce poverty, has stopped investing in fossil fuels projects since 2014. Likewise, the European Investment Bank stated that it "will end financing for fossil fuel energy projects from the end of 2021".

tive of recipient countries, adopting a provision in export finance policies that allows support for electricity supply projects deemed necessary in contexts of severe energy poverty could ensure that human development and access to energy are not jeopardised.

Such provisions should, however, not be used as loopholes to delay the implementation of necessary climate transition policies; they should only be employed when no alternatives are commercially or technically available. Any exception should also be coupled with ambitious greenhouse gas emissions thresholds and mitigation plans.

Recommendations

Sweden has an opportunity to be a leader on policies for climate and export finance. To achieve this, it should:

- Domestically, ensure coherence in all aspects of climate policy and adopt a whole-of-government approach to climate change. This includes ending export finance support to overseas fossil fuel energy projects and recognising the need for a just transition;

- Internationally, help establish a coalition of countries committing to stop export financing of fossil fuel energy projects ahead of the November 2021 UN Climate Change Conference (COP26) in Glasgow;

- Within the OECD, advocate for the introduction of a new Sector Understanding on restrictions to oil and gas export finance, as well as for strong climate provisions throughout the OECD Arrangement.

Appendix 1

Transactions related to oil and gas supported by EKN, January 2019 to April 2021

Note: EKN's exposure to fossil fuel energy projects between January 2019 and April 2021 amounted to less than 1 percent of EKN's total transactions.

Year	Type of guarantee	Amount in MSEK	Sector	*Country*
2019	Supplier credit guarantee (*leverantörsgaranti*)	4	Oil	Singapore
2019	Export loan guarantee (*långivargaranti*)	715	Natural gas	Argentina
2019	Supplier credit guarantee (*leverantörsgaranti*)	153	Oil	Mexico
2019	Supplier credit guarantee (*leverantörsgaranti*)	8	Natural gas	Mozambique
2019	Supplier credit guarantee (*leverantörsgaranti*)	Not disclosed due to secrecy	Natural gas	Mozambique
2019	Counter guarantee (*motgaranti*)	Not disclosed due to secrecy	Oil	Sweden / Singapore
2019	Supplier credit guarantee (*leverantörsgaranti*)	21	Natural gas	Saudi Arabia
2020	Supplier credit guarantee (*leverantörsgaranti*)	3	Oil	Singapore
2020	Supplier credit guarantee (*leverantörsgaranti*)	Not disclosed due to secrecy	Oil	Singapore
2020	Supplier credit guarantee (*leverantörsgaranti*)	7	Oil	Singapore
2020	Counter guarantee (*motgaranti*)	20	Natural gas	Sweden/Taiwan
2020	Counter guarantee (*motgaranti*)	19	Natural gas	Sweden /Taiwan
2020	Counter guarantee (*motgaranti*)	3	Natural gas	Sweden /Taiwan
2020	Counter guarantee (*motgaranti*)	3	Natural gas	Sweden /Taiwan
2020	Counter guarantee (*motgaranti*)	9	Natural gas	Sweden
2021	Supplier credit guarantee (*leverantörsgaranti*)	40	Oil	Mexico
2021	Export loan guarantee (*långivargaranti*)	71	Oil/ Natural gas	Saudi Arabia
2021	Supplier credit guarantee (*leverantörsgaranti*)	9	Oil/ Natural gas	Saudi Arabia

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